

## **A Global Perspective on Contemporary Social and Economic Security Challenges and Opportunities**

Buenos días damas y caballeros.

It is truly an honor and a privilege to be invited to address you this morning. We live in a world of continuing change and progress, particularly with respect to economic, social and political conditions. Such changes present many challenges and opportunities for the actuarial and related professions. Every nation will seek to achieve its objectives for retirement income support and economic security in terms of its own particular social, economic, and political conditions, as well as the culture and history of the nation. It is, nevertheless, informative to review the international landscape to discern what might be useful or applicable from the experiences of other nations with similar objectives regarding the provision of old-age income support and security. Today, I would like to take this opportunity to talk about some contemporary challenges of economic and social development from a global perspective. These major challenges include poverty alleviation, old-age income provision, human rights issues, employment opportunities, and workforce participation. In the context of these broad social and economic development issues, I would like to focus more specifically on social security and pension challenges and opportunities. These issues are truly global in nature; they transcend national and regional boundaries and apply in varying degrees to all nations around the world. Let me start with a brief introduction to the major organizations that represent the global leadership on social and economic policy development. The major institutions are the United Nations, the World Bank, the International Monetary Fund, the International Labour Organization, the World Health Organization, the World Trade Organization and regional development banks such as the Inter-American Development Bank. And in our specific area of interest as actuaries, I would also mention the International Actuarial Association and the International Social Security Association.

The United Nations is a global association of governments organized for the purpose of facilitating cooperation in international economic and social development, law, security, and social equity. There are sixteen Agencies of the United Nations that coordinate their activities through the UN Economic and Social Council including: *United Nations Educational Scientific and Cultural Organization* (UNESCO); *World Health Organization* (WHO); *International Labour Organization* (ILO); *International Monetary Fund* (IMF); *World Bank Group*; and the *United Nations Industrial Development Organization* (UNIDO); These Agencies operate on a supranational basis to address global economic and social issues that transcend national boundaries.

While the UN needs to adapt to changes in the world's social, economic and political conditions, the provisions of the UN Charter remain paramount. The drafters of the UN Charter understood the need for global economic formulation

to be a prime responsibility of the UN and, for this reason, the Charter assigns to the UN the central role for global macro-economic policy and strategy formulation and guidance. Article 1(3) of the UN Charter includes among the purposes of the United Nations, achievement of international cooperation in solving international problems of an economic, social, cultural or humanitarian character.

The World Bank, the International Monetary Fund (IMF) and the World Trade Organization (WTO), have a powerful influence on global development, economics and trade. These three institutions are agencies of the United Nations and originated with the 1944 Bretton Woods Agreement. The World Bank Group includes the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) and the International Development Association (IDA).

IBRD provides loans or grants to member countries for specific projects that are typically linked to implementing policy changes in the development of the client country's economy. The World Bank's development programs are mainly targeted in the areas of infrastructure development, environmental protection, rural and agricultural development, human development and protection, and institutional governance and development. IBRD aims to reduce poverty in middle-income and poorer countries by promoting sustainable development through loans, guarantees, and by providing analytic and advisory services. IFC is the private sector investment entity of the World Bank Group; it invests in sustainable private enterprises in developing and transition countries without accepting government guarantees; it provides equity, long-term loans, structured finance and risk management products, as well as technical assistance and advisory services. IDA provides favorable financing to the world's poorest countries. IDA's interest-free credits and grants, financed by contributions to IDA from donor countries and IBRD's net income transfers, are vital because these poorest countries have little or no capacity to borrow on market terms.

The World Bank's strategic planning initiatives are based on the goals of supporting the creation of a favorable investment climate and empowering the world's poor people. These initiatives include support for sustainable development, improved infrastructure, private sector development, job creation, delivery of social services, and sound governance. The major emphasis of the bank's recent activity has been in the areas of poverty reduction, debt relief and specific Country Assistance Programs.

The United Nations Millennium Development Goals (MDG) set the broad framework for much of the World Bank's development work. There are eight MDG's: Eradicate Extreme Poverty and Hunger; Achieve Universal Primary Education; Promote Gender Equality and Empower Women; Reduce Child Mortality; Improve Maternal Health; Combat HIV/AIDS, Malaria, and Other Diseases; Ensure Environmental Sustainability; and Develop a Global Partnership for Development. In terms of reducing poverty and inequality, the

Bank works with countries to prioritize their needs, articulate development strategies, and select financial instruments appropriate to fund those needs.

The IMF advises and assists member countries in implementing economic and financial policies that promote stability, reduce vulnerability to crisis, and encourage sustained growth and high living standards. It also promotes dialog among member countries on the regional and international consequences of their economic and financial policies, and reviews global economic trends and developments that affect the health of the international monetary and financial system. Promoting economic stability is partly a matter of avoiding economic and financial crises. As recent experiences have shown, crises can destroy jobs, reduce incomes, and cause human suffering, both nationally and beyond a country's borders if the crisis spreads. But economic stability also means avoiding large swings in economic activity, high inflation, and excessive volatility in exchange rates and financial markets. Any of these types of instability can increase uncertainty and discourage investment, impede economic growth, and hurt living standards. A dynamic market economy inherently involves some degree of instability, as well as gradual structural change. The challenge for policymakers is to minimize this instability without reducing the ability of the economic system to raise living standards through increasing productivity, economic efficiency, and the employment opportunities that it generates. Economic stability is also fostered by robust economic and financial institutions and regulatory frameworks that support transparency of financial transactions in the government budget, central bank, and the public sector, along with strong standards and systems for accounting, auditing, and data provision. The IMF also closely monitors economic and financial developments at the regional and global levels; among the initiatives used to promote economic stability are the IMF's assessments of countries' vulnerabilities to crisis and, in collaboration with the World Bank, the IMF conducts assessments of countries' financial sectors including capital market surveillance. The IMF also develops and promotes standards and codes of good practice in economic policymaking. The IMF helps countries strengthen their capacity to design and implement sound economic policies. The IMF provides advice and training on a range of institutional and policy issues, including fiscal, monetary, and exchange rate policies, the regulation and supervision of banking and financial systems; the development of statistical systems; and of associated legal frameworks. Twenty-first century globalization is presenting the global community with new challenges. The IMF has an important role in fostering international cooperation and helping individual countries to meet these challenges.

The International Labour Organization (ILO) is a United Nations agency devoted to advancing opportunities for men and women to obtain productive work in conditions of security, equity and dignity. Its main aims are to promote rights at work, encourage employment opportunities, enhance social protection and engage in dialog on work-related issues. The ILO brings together representatives of governments, employers and workers to jointly shape policies and programs.

The ILO is responsible for developing, implementing and supervising International Labor Standards. In cooperation with its 181 member nations, the ILO seeks to ensure that labor standards are respected in both principle and practice. The ILO provides technical assistance programs to governments, workers and employers worldwide, particularly in developing nations. Work is central to people's well-being in a globalized world economy. In addition to providing income, work can pave the way for broader social and economic advancement, thus strengthening individuals, families and communities. Such progress, however, depends on working conditions that are decent and that represent the aspirations of people during their working lives. These aspirations include opportunities for work that is productive and that delivers a fair income, security in the workplace and social protection for families. They also include better prospects for personal development and social integration, and freedom for people to express their concerns, organize and participate in the decisions that affect their lives. Paramount among these aspirations is equality of opportunity and treatment for all men and women. Providing work opportunities is the key to alleviation of poverty and is the means by which individuals may share in the gains brought about by increased international economic integration. Extending opportunities for decent work to more people is a crucial element in making globalization more inclusive and fair. For these reasons, creating employment opportunities is at the heart of global development policy.

The World Health Organization (WHO) is the coordinating authority on international health matters within the United Nations system. WHO experts help countries to address public health issues and, as a part of this process, the WHO promulgates health guidelines and standards. The WHO also supports and promotes health research. Working in conjunction with the WHO, national governments can address the challenges of global health problems and seek to improve the health and well-being of their populations. At the United Nations Millennium Summit in 2000, 191 countries pledged to address the ambitious tasks of tackling poverty and ill-health and improving people's lives by 2015. Derived from the Millennium Declaration, these tasks are known as the Millennium Development Goals (MDG). Health-related issues are at the center of the MDG agenda. Three of the eight MDGs are directly health-related issues: reducing child mortality; improving maternal health; and combating HIV/AIDS, malaria and other diseases.

The World Trade Organization (WTO) was established in 1995 as a successor to the General Agreement on Tariffs and Trade (GATT). WTO provides a forum for trade negotiations, administers trade agreements, monitors national trade policies, handles trade disputes, and provides technical assistance for developing countries. The main purpose of WTO is to ensure that trade flows as smoothly, predictably and freely as possible in accordance with global rules of trade between nations, resulting in a more prosperous, peaceful and accountable economic world. At the heart of the WTO multilateral trading system are the WTO agreements that are negotiated by a majority of the world's trading nations.

These agreements represent the ground-rules for international commerce and trade that guarantee WTO member countries important trade rights. Under the WTO agreements, the guiding principle is trade without discrimination; this implies that imported and locally-produced goods should be treated equally; the same principle applies to foreign and domestic services. Countries cannot discriminate between their trading partners and are required to follow the principle of most-favored-nation by extending any special concessions that are granted to any trading partner to all trading partners without discrimination. Lowering trade barriers is one of the most obvious means of encouraging trade; such barriers include customs duties, tariffs, and measures such as import bans or quotas that restrict quantities selectively; other indirect barriers to trade include administrative procedures and exchange rate policies. Other guiding principles of the WTO include encouraging freer trade through negotiation, achieving predictability through binding commitments and transparency, promoting fair competition, and encouraging development and economic reform.

In 2003 the International Social Security Association (ISSA) published a significant paper *Ageing and Social Security*. This paper identified the main challenges of ageing societies: Enhancing labor market opportunities; Reversing the trend towards early retirement; Meeting challenges of insecure employment; Limiting individual risks in preparing for retirement; Securing adequate income for old-age through the mix of public and private arrangements; Determining the role of the State in an ageing society; Ensuring gender equality in pension provision; Providing sustainable health and long-term care to an ageing population; Addressing the challenges of ageing in low-income and middle-income countries; and making Social Security a prerequisite for the financial security of individuals in ageing populations.

Much of the discussion on old-age pension reform and cost containment in health care has revolved around the issue of economic sustainability in the face of ageing populations. The future viability of ageing societies will inevitably depend on whether the provision of social security is economically sustainable. Of equal importance, is the social sustainability of an ageing population. How can Social Security systems be adapted to the challenges and opportunities of ageing societies around the world? How can the social security of the population be ensured in an efficient and equitable way? The future of ageing societies depends on the success with which economic and social sustainability can be combined in a comprehensive approach to social security.

In recent years the World Bank has published a number of influential reports on the topic of pension reform. *Averting the Old-Age Crisis: Policies to Protect the Old and Promote Growth* (1994) advocated a system of mandatory individual accounts as one of the principal pillars of a pension system. *Old-Age Income Support in the 21st Century: An International Perspective on Pension Systems and Reform* (2005) reviewed the experience with pension reforms over the previous decade and presented an updated and broader view of pension reform

issues based on the lessons learned from the experiences of the World Bank in implementing reforms in a number of countries. The International Actuarial Association presented a response from the global actuarial profession to the World Bank's 21<sup>st</sup> Century vision at a 2006 International Congress of Actuaries in Paris. This response commented on the problems and dangers associated with some of the World Bank's reforms including the Chilean and Swedish Social Security Systems and presented an objective assessment of the Defined Contribution and Notional Defined Contribution arrangements that, to a great extent, the World Bank has advocated as a panacea for pension reform around the world.

There are significant challenges presented by the demographic trends that are producing declining ratios of working-age populations to retired populations in many countries, due to increasing life expectancy and falling fertility rates. These challenges have produced a focus on reforms, both structural and parametric, including contribution adjustments, benefit adjustments, changes to retirement ages, financing methods, and funded complementary arrangements.

It is often said that demography is destiny. Demography influences economics: economics influences politics: and politics influences social policy. Together, these forces drive the relative wealth and geopolitical power of nations. In a global context, the two main demographic factors, declining mortality rates and birth rates, impact the future population size and age structure of individual nations, geographic regions and the whole world. The rate of world population growth has fallen by more than 40 percent since the late 1960's. Demographers at the Institute for Applied Systems Analysis predict that the global population will peak at around 9 billion by 2070 and then start to contract. Some 59 nations, comprising about 44 percent of the global population, are not producing sufficient live births to avoid population decline. The changing economics of family life is the primary factor influencing falling birthrates. The world's current generation of women of childbearing age is producing children at a rate about only one-half that of women two generations earlier. In Mexico, fertility rates have fallen substantially and the rate at which the Mexican population is ageing is about five times greater than for the United States. According to United Nations projections, Mexico's median age will increase from about 22 to 42 over the first half of this century. These global demographic trends impact the world's economy and the geopolitical balance of power. Slower population growth is credited with the economic boom in Japan and other Asian nations from the 1960's onwards. In East Asia, the working-age population increased four times faster than the non-working population of children and seniors between 1965 and 1990. A lesser emphasis on family formation and raising children was a key factor in providing a large increase in the female labor force and freeing up social and economic resources for growth and investment. China's recent rapid industrialization is facilitated by its restrictive one-child family policy. Throughout the Middle East, the ageing of populations is making available more resources for infrastructure and industrial development that otherwise would be committed to dependent

children. Ageing populations bring gradual changes in economic, political and social policy matters. Older populations place more emphasis on issues such as health care and retirement income and savings. Political activism and violence are less in evidence among older populations than younger populations.

The 2005 World Bank report *Old-age Income Support in the Twenty-first Century* was both significant and influential. At the heart of this report was a recommended multi-pillar approach for the structure of pension systems composed of a flexible and discretionary combination from among five basic elements:

- A non-contributory demogrant or social pension that provides a minimal level of protection
- A contributory system linked to earnings to replace some portion of income
- A mandatory system of individual savings accounts
- A voluntary system that is flexible and discretionary that may take many potential forms, defined benefit or defined contribution, employer-sponsored or individual
- Informal financial and non-financial support from intra-family or inter-generational sources to the elderly including access to housing and health care

Together these five elements have become the World Bank's global standard or framework for comparative assessment and reform purposes in advising on old-age income security in countries where its influence is sought. The World Bank also presented four principles to be considered in setting the primary goals of a social security system:

- Adequacy
- Affordability
- Sustainability
- Robustness

An adequate system provides benefits to the whole population that are sufficient to prevent old-age poverty in addition to providing a means to smooth lifetime consumption for the population. An affordable system is within the capacity of society and individuals and does not displace other social or economic imperatives or have untenable fiscal consequences. A sustainable system is financially sound and can be maintained over a foreseeable horizon under a broad set of reasonable assumptions. A robust system has the capacity to withstand major shocks including those attributable to economic, demographic and political changes or trends.

Over the last 20 years, the World Bank has made more than 200 loans, involving more than 60 countries that were related to pension reform and development. The bank has supported a diverse range of pension reforms within the Bank's multi-pillar framework. The bank has been influential in making several different types of pension system and social security reforms, including:

- Parametric reforms that retain the basic structure of benefits, public administration, and the unfunded nature of the system, but where key elements of the parameters that define benefits, contributions and eligibility conditions are modified.
- Reforms that change the structure of benefits that retain public administration and the unfunded nature of the system, but introduce concepts such as the non-financial or notional defined contribution arrangements into the system.
- Market-based reforms that provide fully-funded benefits of either a defined benefit or defined contribution nature under private management arrangements
- Reforms that combine public pre-funding and public administration, again based on either defined benefit or defined contribution concepts.
- Multi-pillar reforms that diversify the structure of benefits, funding and administration of the system.

It is the stated policy of the World Bank to include in its reform proposals the needs of the main target population groups in client countries, including: formal sector workers, informal sector workers, and the lifetime poor. Some observers have suggested that the World Bank has used its role as lender to impose its views and opinions relating to pension reform and system structure on client countries as a condition of making funds available for social and economic development projects. The World Bank is sometimes criticized for its somewhat doctrinaire approach to economic and social policy development and in particular with its views in favoring funding and individual account arrangements. A particular area of contention relates to the World Bank's favoring of the notional defined contribution concept. The World Bank's goals of implementing adequate, affordable, sustainable and robust systems for providing retirement income, or old-age income support, in the terminology of the bank, constitute the bank's primary objectives. The bank also has secondary development goals that are important influences on the bank's policies. These secondary development goals are intended to create positive developmental outcomes by minimizing the potential negative impacts on labor markets and macroeconomic stability, while emphasizing positive impacts through increased national saving and financial markets development.

Let me now turn to the next institution that I referred to earlier in my list of important sources of research and influence, namely the International Labour Organization (ILO). The ILO is an agency of the United Nations, as is the World Bank.

The ILO has a well-documented set of principles and standards that address the following five key objectives for social security:

- The extension of coverage to all members of the population
- Protection against poverty in old-age, during disability, or on death of the wage earner, for all members of the population.



- Provision of an income, in replacement for earnings lost as a result of voluntary or involuntary retirement, for all those who have contributed
- Adjustment of this income to take account of inflation, and at least to some extent, of the general rise in living standards.
- Creation of an environment for the development of additional voluntary provisions for retirement income.

The ILO translates these philosophical principles into formal International Labour Standards. As an example, the ILO advocates a target minimum level of benefits to provide income replacement in retirement at 40 percent of earnings. The focus of the ILO is very much on the primary social objective of providing adequate retirement income. Whereas, by contrast, the World Bank's approach is also motivated and influenced by economic policy objectives and broad development goals. In general, for basic social security systems, the ILO favors defined benefit structures and unfunded pay-as-you-go financing arrangements.

There is one particular topic that I would like to explore with you as a major challenge in the area of social security and pension reform: the gender-related issues affecting women. One of the United Nations Millennium Development Goals is to promote gender equality and empower women. Many of you will be familiar with the excellent book *Lessons from Pension Reform in the Americas* by Professor Tapen Sinha and Stephen Kay; two chapters in that book are devoted to this issue; one chapter discusses the gender impact of social security reform in Latin America; the other chapter discusses pension reform and gender inequality. This is also an area that we have researched at the American Academy of Actuaries resulting in the publication of an Issue Brief *Women and Social Security* in June 2007. This Issue Brief was related to the United States Social Security system, but many of its findings and conclusions are relevant in a global context.

In the United States, Social Security provides benefits on a gender-neutral basis. Benefits are based on an individual's earnings record, employment history, and family composition. However, gender-related differences in the United States work environment mean that, in reality, Social Security provides different levels of retirement security for women and men. When the current benefit structure was set up, more than seventy years ago, the traditional roles of men in the family as primary wage earners and women as primary child care providers were well established. The system provides the highest benefits relative to contributions to married couples with a primary wage earner, presumed to be the husband, and their children. As women have taken on increasingly larger roles as heads of families or as primary or co-equal wage earners in their families, situations frequently arise where Social Security provides lower benefits for the same contributions, or requires significantly higher contributions with little, if any, increase in benefits compared to the traditional family. Factors that can affect

these differences in the benefits women and men receive from Social Security include:

- Employment history and earnings. Women tend to have more frequent breaks in employment due to child-bearing, child care, or care of elderly parents. When they are working, women on average earn less than their male counterparts. Thus, women generally receive lower Social Security benefits based on their own earnings histories, as compared to men.
- Disability. Unpaid homemakers and caregivers do not qualify for coverage because they do not earn taxable wages, so some women are less likely to have sufficient recent employment to be insured for purposes of Social Security disability insurance benefits. If they qualify, women are likely to get lower benefits than their male counterparts.
- Life expectancy. Women, on average, live longer than men. Therefore, a woman who retires at the same age as a man can be expected to collect benefits over a longer period. The majority of women have fewer assets than men and are more dependent on Social Security.
- Marital Status. A higher proportion of women than men never marry. As a consequence of longer life expectancy, and the fact that women are often younger than their spouses, women on average are more likely than men to become widowed before or during retirement. In addition, older women who lose a spouse are less likely than men to remarry. All these factors mean women are likely to spend longer periods during retirement unmarried, and these periods are likely to fall at the more advanced ages. Social Security survivor benefits are designed to provide retirement security to widows and widowers, but provide no protection for the never-married or for divorcees if the marriage lasted fewer than 10 years.

The United States Social Security system recognizes differences in financial circumstances among the workers and dependents it covers. As such, the current Social Security program provides certain safety net or social adequacy features to ensure that the less well off get enough benefits for retirement security. Although these features are not targeted at women, women often benefit from them more than men because of the factors mentioned previously. Some Social Security reform options currently being contemplated would change the social adequacy components of the program, with potentially disproportionate effects on women relative to men.

The Academy's Issue Brief discussed the relative differences in the factors affecting men and women, as well as how these differences contribute to disparate benefits under Social Security. This includes the impact on the average woman of social adequacy provisions of the current Social Security program and various proposals to reform Social Security, including individual accounts. This combination of factors means that the average woman has a higher risk of having insufficient income or depleting savings in her retirement years.

Recent pension reforms in Chile and the United Kingdom, for example, have acknowledged the need to recognize the special circumstances of women and to implement measures that are more equitable in providing adequate income support to women in old age.

There are many other challenges and opportunities facing the actuarial profession, not only in Mexico, not only in Latin America but in a truly global context. The available time permits me to list just a few of these challenges: ensuring the efficiency and adequacy of defined contribution systems where these have been adopted as part of reforms; extending social security coverage to a much greater number of individuals particularly for workers in the informal economy; ensuring the deliverability of lifetime income during the post-accumulation phase; strengthening financial institutions that provide for delivery of annuities; and providing robust protection against the risks of longevity, inflation and market-related risks such as interest rate changes and securities market valuations. We are fortunate in being members of a profession with the essential skills and dedication to tackle these challenges and explore the opportunities that they present. I hope that I have set the stage in broad economic and social terms for the distinguished speakers who will follow in today's program and who will address some of the more immediate challenges and concerns for the profession here in Mexico.

Thank you.